RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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DILEMMA: I've written many times that with the amount of debt now built into the US economy there are only two choices -- "inflate or die." There's just no painless way out of the debt-mess we're in. Where are we now in this dilemma? We're right in the middle, betwixt and between. Partly, we're dying because this economy, despite massive federal deficits over $1 billion a day, can't really get rolling.

On the other hand, with the Fed flooding the banks with liquidity, it's obvious that our servants in Washington are trying desperately to re-inflate. According to the Fed's own Federal Reserve Statistical Release (Mar. 10), the total credit market debt in the US is now just a billion short of **$15 trillion.** And the true calendar 1993 federal deficit came in at $470 billion or **$1.28 billion a day.**

The pressure of this massive debt edifice is deflationary. At an average interest cost of 7%, the interest cost to carry America's $15 trillion in debt is a staggering $1 trillion a year, equal to one fifth of our GDP. That kind of interest-payment cost can only be "handled" through inflation. I don't care what the Fed or Clinton or anyone else says, the US must inflate. Let me say it again, we'll either "inflate or die."

If we succeed in inflating, it will be bullish for gold, bearish for bonds, possibly (but with a big maybe) bullish for stocks, bullish for real estate, and long-term bearish for the dollar. But if we deflate, you'll see the damnedest bear market of your lifetime.

THE MARKET: There have been a lot of sell-offs and collapses among individual stocks and stock groups over the past few years -- even while the major stock averages were recording new highs. Is that enough? Can individual losses substitute for a major correction? Can they even substitute for a bear market? Unfortunately, the answer is, "No, it's not that easy."

I just received *Investment Quality Trend's* latest tabulation for the Percentage of Undervalued Blue-Chip Stocks. I must admit that I sort of gasped. The Percentage has now dropped to **6%,** the lowest figure ever.

This is a statistic that I post on page 1 of every issue of *Dow Theory Letters.* At bull market tops this Undervalued Percentage tends to run around 10% to 12%. But what about today's 6%? That 6% means that of *IQ Trends'* universe of 350 blue-chip issues, only 6% or 21 stocks are now classified as undervalued! Let's face it, this market is EXPENSIVE.

On the other hand, at bear market bottoms roughly 80% or more of these same 350 blue-chip stocks are classified as undervalued. Believe me, we'll see that figure again some time -- but when?

Every bull market in history comes to an end. Every bull market eventually dies. That's hard to believe in an extraordinary period like the one we're in, but as night follows day, bear markets do follow bull markets.

So why not have fun -- right up to the time when the bear finally emerges from his lair? Why not just keep on buying? Fine with me. There's only one problem. History tells us that when we're paying $36 for one dollar of S&P dividends (which is what we're now doing), the odds on our making money in the stock market are poor. In fact, the odds are rotten.

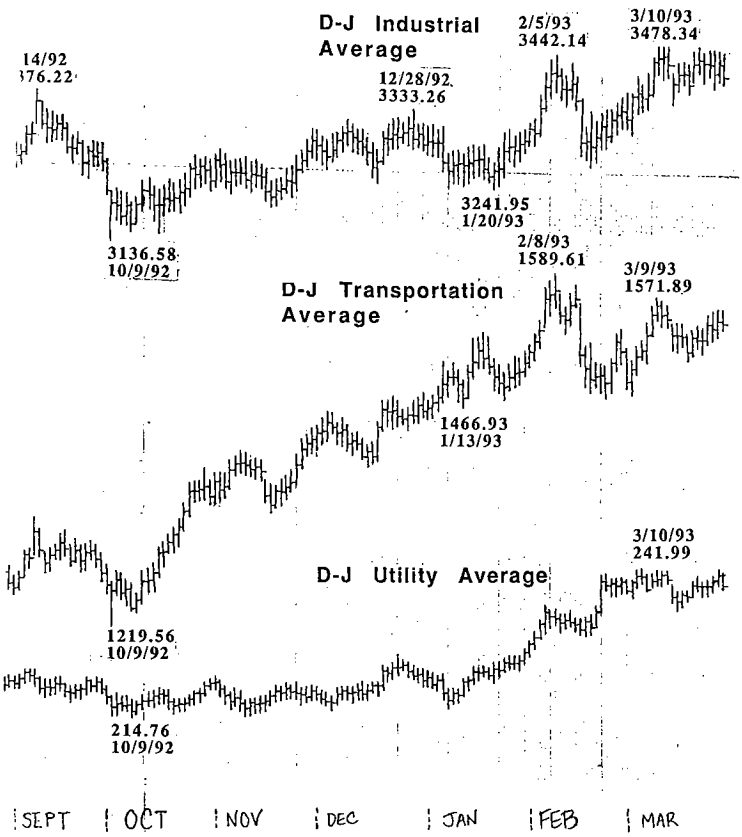
Mar. 19 DJIA 3471.58; PTI 3754; A-D Ratio -4.92
Mar. 26 DJIA 3439,98; PTI 3750; A-D Ratio -5.12
Dow Yield: 2.81%; Dow Price/Earnings: 35.6
Dow 200-day MA: 3305; Dow 30-day MA: 3413
Dow Times Book Value: 2.64; PTI 89-day MA: 3698
Percentage of Undervalued Blue-chips: 6%
Low Risk Buy Index: +84

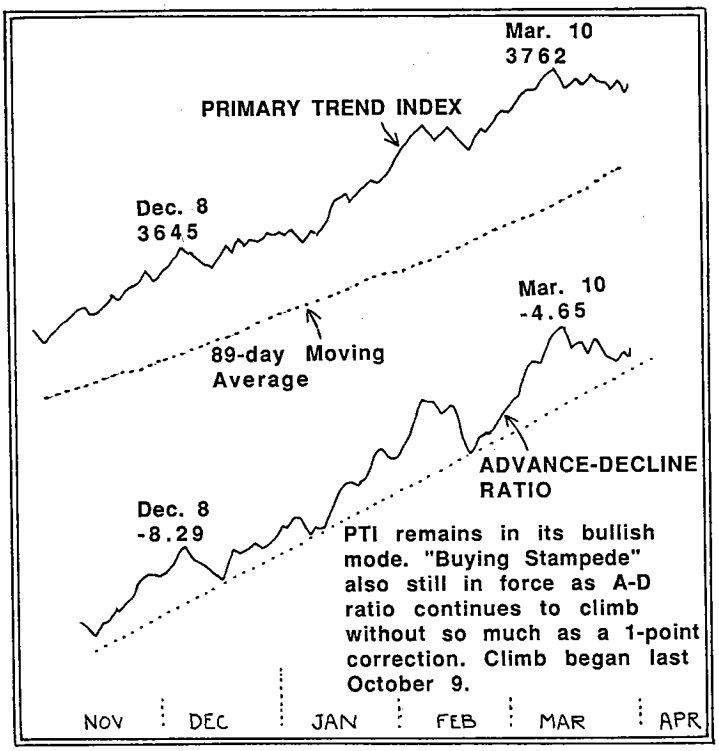
Let me put it another way. If you buy say 10 good, well-researched stocks in this area, the odds are that a year from now the average price for these 10 good stocks will be lower.

When stocks become too expensive they also become very sensitive to any kind of shock. Example: Merck is a great company; nobody questions that. But at its recent high, MRK was selling at eight times sales (sales, not earnings). Then came the Clinton "pressure" on the pharmaceutical industry and Merck dropped from 58 to below 34. Merck's still a great company, but it isn't dirt-cheap even at 34. But that's what can happen to a stock or the stock market when people become too optimistic and pay too much for a stock or the market.

Veteran market people know that the big swinger, the big mover, in the stock market is the perception of future earnings. Perception translates into price/earnings, or what investors are willing to pay for earnings. Thus, at the start of a given bull market the price/earnings for the Dow may be as low as 6. At the top of the same bull market, price/earnings may have risen to 35 (where they are now). So earnings may be rising, but it's the multiple that investors are willing to pay for those earnings that is the big mover.

The same process works in reverse in a bear market -- as earnings decline. In a big bear market investors will have turned stone bearish, and consequently price/earnings ratios will collapse.





That's the process that takes stocks to ridiculously low levels at a bear market bottom.

As this is written, the "buying stampede" that I wrote about in the last Letter is still in force. The buying stampede started last October 9, and it has already moved the advance-decline ratio up over five points. The buying stampede will remain in force until such time as the advance-decline ratio drops one full point or more (see page 2 chart).

My Primary Trend Index remains in its bullish mode. You may or may not like this market, but as long as the PTI is bullish, you better think twice or three times about putting out a collection of shorts. A rising PTI tells you that it's a lot easier to play the "up" than the "down" side of the market.

Meanwhile, I've been watching the CRB Commodities Futures Index, which is near its high for the year. I'm watching the inflation figures which show that the "core inflation" rate has been running at a 6% annualized rate for two months in a row. I'm watching the sky-high lumber, the over-$20 oil, the record highs in cattle, and the rally in selected grains. Commodity mavens believe that the commods are at or close to a five-year cyclical low. Could inflation be "just around the corner"? If that's the case, expect lower bonds and higher long-term interest rates.

For now, however, the market appears simply to be working off an oversold situation. Personally, I 'm amazed the market is taking the Clinton program as calmly as it is. To me, Clinton and Hillary add up to a disaster. But don't panic -- the market doesn't run on Richard Russell's opinions, it runs on two massive forces which we call supply and demand.

THE PICTURE: Hey, how're we doing? Well, to be honest it's getting kind of crazy. On March 11 President Clinton said that the $37 billion in savings from the military that he wanted in 1997 might not materialize due to the Russian situation. Then a day later Treasury Secretary Bentsen said that the RTC needs some more money, actually, another $45 billion, to wind up the S&L bailout program (52 additional S&Ls will be going belly-up in the next six months). And then there's Hillary, working on her hush-hush health-care plans (and nobody knows how much those plans will cost).

On March 18 the House, voting along party lines, passed Clinton's economic program, but of course the Senate will have to kick around the Clinton "tax-us-to-prosperity" program before it can become law.

So again, how're we doing? Well, a lot depends on your viewpoint. From my viewpoint, I note that we'll be adding roughly $1.5 trillion to the federal debt by 1998 (but it could be more if interest rates go up). That's not too good is it?

And the problem for the politicians is this -- Clinton has four more years to soothe the voters with his brand of in-your-face, to-the-people salesmanship. But House members and 22 Senators have only two years before they have to face re-election. So if taxes go up (which they will) but there's no real progress on the deficit, these politicians in '98 will have to deal with a very angry electorate, and the odds are that those pols will be out on the street looking for real jobs. Gosh, is that why even the liberal Dems have been pushing Clinton for more cuts?

INVESTMENT POSITION: El Toro, the long-lived bull, remains in the box. The paradox: the market is selling at extremely high multiples (in normal language that means "it ain't cheap"). But it's a market that, from all appearances, doesn't want to go down.

So what do you do with a super-expensive stock market and a bond market that looks toppy? Answer: You treat it with kid gloves. In other words, I wouldn't take out a bank loan (assuming you could get one) and load up with stocks. And yet, a selected number of stocks still act well (including the finance stocks and more particularly the bank stocks). Yes, I know that a thousand analysts are telling you that stocks are still a "buy," and I know that "leading authorities" are telling you that minuscule dividends don't matter, and I know that "this time it's different." But I still want to be careful and basically conservative here.

If the money is piling up and you've got to do something, well, my old friend, Charles Maxwell, senior energy strategist for C. J. Lawrence, Inc., probably knows more about oil and oil stocks than anybody around. In his March 5 mailing, Charlie states, "I have not recommended an oil or gas company since January of 1981. But every cycle eventually turns." So saying, Mr. Maxwell likes Marathon Oil, Phillips Pete., Unocal, and in oil service he likes Western Co. of N.A., Smith International, Baroid Corp. and Tidewater Marine. As I said, Charles Maxwell knows his oils.

In bank stocks I like Bankers Trust, Bank of New York, JP Morgan and NationsBank. The last, NB, is very aggressive and just took over Chicago Research and Trading Corp., a huge and profitable option and futures company, which should add a pile to their future earnings.

My overall view: maybe have 20% in selected stocks here and be ready to exit if the PTI turns bearish.

The gold stocks have been moving to highs for the year. My choices here would be Amer. Barrick, Pegasus, Placer Dome and Royal Oak (RYO). And for risk-takers, ASA. But c'mon, when gold rises, ALL the gold stocks rally. Now if the metal would just push into the 335-340 area, we would, for sure, see some upside fireworks.

GOOD NEWS, BAD NEWS: Here's an interesting way of putting it, with thanks to *ISI's* Ed Hyman for the idea (I added a few items of my own).

Clinton's Dream:
(1) The economy today is moving towards 4% growth.
(2) Taxes are increased but spending growth is contained.
(3) The economy slows but continues to grow at roughly 3%.
(4) Bond yields decline significantly as bonds spiral higher.
(5) Stock prices trend ever higher.

(6) The federal deficit drops to $190 billion in 1995 amid cheers from the populace.
(7) A grinning, hand-shaking Clinton cuts middle-income taxes in '95.
(8) The stock market goes wild, and the economy accelerates into 1996.
(9) Clinton is reelected. Perot lapses into uncharacteristic silence. Jack Kemp says he will skip the '96 election, but will run in the year 2000. Plans for a George Bush library are called off through lack of gift-funds.

Clinton's Nightmare:
(1) The economy remains fragile.
(2) Taxes are increased, but the "wealthy" aren't cooperating -- they just don't want to pay (as Clinton puts it) "their fair share."
(3) A raft of new federal programs are instituted.
(4) Congress can't get together on substantial budget cuts.
(5) The economy slides back into recession.
(6) With the recession on, tax receipts ("contributions") come in sharply below earlier estimates.
(7) In view of the renewed recession, Clinton calls for a cancellation of many budget cuts ("but fellow Americans, the cuts will definitely be reinstated at a more opportune time").
(8) Federal spending escalates out of control.
(9) The deficit in 1996 is $600 billion.
(10) Clinton is voted out of office.
(11) George Bush writes a book entitled "Give Me Back the '80s." Ross Perot, running on an "I told you this would happen" program, defeats Republican Jack Kemp, and becomes our new President. The nation goes berserk with liberals crying "Fascism" and "Perot-noia."

AH, SUCCESS, PERFECTION: Every year thousands of new companies are formed. Most will struggle, a great many will die. And a few will do very well. *INC* magazine (March) presented a study of the nation's "fastest-growing" start-ups. The magazine wanted to know whether there was a common denominator in the success of these companies. *INC* uncovered 8 correlations or common "rules." Here they are:

(1) The successful start-ups rely on team efforts.
(2) They're headed by people who are experts in their line of work.
(3) They're headed by experienced people who have started other businesses.
(4) They're headed by men (at least the fastest-growing companies are, no offense to the women).
(5) They're disproportionately manufacturers and they're high-tech.
(6) They're better financed "but not by much."
(7) They're not owned by the founders alone (many of the builders don't own a majority of the company).
(8) Their markets are not just local.

All right, as long as I've gone this far, I want to repeat a piece that I've had a great many requests for over the years. This is my article on the "perfect business." It's a piece I first published in the early 1970s, I repeated the piece in Letter 881 and again in Letter 982. Obviously, no company can boast all these plusses, but I think the list gives you an idea of what to look for in the ideal company. The list should also give you an idea of how close to ideal your own company is or how good a concept the company you want to start is.

As far as business experience and my background for writing this piece, I've had a number of jobs. And I've run a number of side-businesses, and never lost money in any of them. After graduating from New York University in 1946, I worked in NYC in the textile business, as a designer, merchandiser and salesman. Believe me, if you can survive and prosper in New York's textile business, you can survive anywhere. Happily, I actually did pretty well.

I've run a book publishing business, I ran a night club for five years, and as you know I've been in the advisory business since 1958. I grew up during the Great Depression, and I've seen very good times and I've seen bad times, very bad times.

My first job (1939) was delivering telegrams for the now defunct Postal Telegraph company. I was 15 years old at the time and was paid by the individual delivery plus tips. I made about $2 a day, but that wasn't bad for a kid in '39. I was a busboy at the Concord Hotel in the Catskills in 1941, and I made about $20 a week. That was the toughest, nastiest work and the longest hours I've ever put in. In 1942 I got a job loading trucks for George W. Button Co. in New York's Harlem (those were the days when a white boy could go to Harlem and come out alive). It was an union job, and I got paid $18.75 for five days plus half-days Saturday.

After the war and after I had finished college I got a job in the textile industry. Times were tough then, the market had collapsed in 1946, and everyone was waiting for the second Great Depression (which, of course, never came). Wall Street was dead, volume was running 2 million shares a day, and being a stock broker meant sitting there watching the tape sputter by, while hoping for a client or two.

So I landed a job in a major textile firm in the sample room at 35 bucks a week (this for an ex-officer in the Air Force and a college graduate), but in the depressed market of 1946 I was happy to have any job. I turned out to be a good designer and salesman and by 1955 I was making $18,000 a year, which was great money in those days. But my fascination was with the stock market, and I spent long hours in the library studying the works of the market masters.

In 1958 I started Dow Theory Letters. I started it with $300 in capital, and a huge boost from *Barron's*, which ran 20 of my articles over the years. My literary mentors were Dow, Hamilton and Rhea, none of whom I had ever met. My living mentor and teacher was the great George Schaefer, a man who inspired me during the '50s, '60s and early '70s.

But back to the original subject, which is the ideal, the perfect business. Over the years I developed a series of criteria for what I term the ideal business, and I list them below. The more of these criteria your new business or new firm (or old firm) possesses, the better off you'll be.

(1) The ideal business sells the world, rather than a single neighborhood or even a single city or state. In other words, it has an unlimited market.

(2) The ideal business offers a product which has an "inelastic demand." Inelastic demand means that almost regardless of price, people want it or need it.

(3) The ideal business sells a product which cannot be easily substituted. Nor can it be copied or reproduced. In other words, it is an original, or an item than can be copyrighted or patented.

(4) The ideal business has minimal labor requirements, the fewer personnel the better.

(5) The ideal business boasts low, low overhead. It does not need an expensive location; it does not need large amounts of electricity, water, etc. Nor does it need advertising, legal advice, large inventories, etc.

(6) The ideal business does not require large cash outlays or major investments in equipment. In other words, the business does not tie up your capital.

(7) The ideal business has cash billings as against terms. The business does not tie up your money with extended and expensive credit arrangements.

(8) The ideal business is relatively free of all kinds of government and industry regulations and strictures (if you're running a business now, you know only too well what I'm talking about).

(9) The ideal business is portable. You can take it (and yourself) anywhere you want, and today you'd probably prefer a state with no taxes (or if you're really, really fed up, you can take your ideal business to Monte Carlo or Switzerland or the Cayman Islands).

(10) Here's one that's frequently overlooked, but believe me it's important. The ideal business is one that satisfies your intellectual and even your emotional needs. In other words, if you own this business you look forward to going to work -- your work is so exciting that when you go on vacations you find that you're bored.

That's it, the Russell list. If you use this list it may help you cut through a lot of nonsense and hypocrisy. And hopefully, this list will help you avoid some bad decisions. None of us own or work for the perfect business. But it's nice to know what to look for and how close we are (in our current situation) to that ultimate fantasy --the ideal business.

NOTES & QUOTES: The Republican position on the Clinton economic program is clear. Disassociate the party from the Clinton program (did you see the full-page disclaimer-ad in the March 23 *USA Today?)*, vote against the program, watch the program go through Congress, watch it kill the economy while boosting the deficit, watch Clinton become a one-term president -- finally, watch the Republican party come back to power in '98.

In his effort to pass his program, Clinton has gone over the heads of Congress directly to the people. There are two reasons why he's doing this: First, the average person doesn't understand the full negative implications of the Clinton program. And second, the average American isn't the one who's going to be hurt most by the plan. No, it's the "over $100,000 income" American who will really pay. Why them? Easy, these wealthier Americans don't have the votes, there just aren't that many of them.

* *

It's not good, but it's happening. In Russia up to 527,000 Communists have been re-registered in the last 12 months, making the group the largest political party. Their goal is a million and a half Communists by the end of '93. As I said -- not good.

To repeat, I thought it was unbelievably stupid when the Russians failed to back the ruble with gold (which would have made it a real currency). When the ruble collapsed, it meant rampant inflation for Russians and a wipe-out of all their savings. The first consideration when you want to establish a new nation is a stable currency. The ruble is now a worthless, piece of paper (650 to the dollar), and the Communists are making hay out of the chaos which has been created.

Insiders consider Boris Yeltsin to be "yesterday's man," actually a stop-gap hero in the history of Russia. The man people are watching is another Boris, 34-year old Boris Nemtsov. Nemtsov is governor of Novgorod, Russia's third largest city. He's turned that city into a bastion of private ownership in only one year. The two Borises are political allies, but the thinking is that the future (if there is to be a democratic future in Russia) belongs to Nemtsov, not to Yeltsin.

* *

The story of how the US constitution was subverted and how the money-creating power went to a private organization, the Federal Reserve, is an amazing one. According to the Constitution (Article 1, section 8) Congress alone has the power "to coin the money and regulate the power thereof." Secondly (article 1, section 10) states that "only gold and silver coin are legal tender in payment of debt." I asked a neighbor who happens to be a lawyer and a professor (he teaches Constitutional law), how this could have happened? He smiled and answered, "The law is what the Supreme Court says it is."

At any rate, I do know this. The founding fathers warned against exactly what has happened to our money and our money creation. The Constitution gave us a free market money system with checks and balances based on precious metals to back the currency. It's obvious that system has been totally subverted. But I want to learn more. I know that I have many brilliant subscribers who are expert in this area. If any of you will kindly supply me with further information on the subverting of the Constitution and the creation of a private money monopoly, I would very much appreciate it. Many thanks.

* *

You want to know how complex and ridiculous the current US tax system is? Get this, *Money* magazine (April) in an exclusive survey discovered that 34 of the 58 senators and representatives on the two tax-writing committees don't fill out their own tax returns (yep, they have to use accountants). And these are the same jokers who dream up our taxes.

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Ed Hyman (*ISI*) tabulates the corporate lay-offs each week. I mean these companies are analyzing their work forces, they're computerizing, they're getting lean and mean, and they're finding out that they can do without. A typical week -- mid-March announcements: Northrop's laying off 2,400; Thiokol unspecified number; WestPoint-Pepperell -- 350; GTE a whopping 26,000; Merck -- 1,000; Centerior Energy -- 1,400; National Geographic -- 800. National Geographic? C'mon, I didn't think they had that many employees. And these are jobs that are lost forever, gone, kaput, finito.

* *

As I've written before, Asians tend to be savers as opposed to the US savings rate which is now running around 4.7%. Singapore's national savings is the world's highest at 43%. Malaysia is 33%, Hong Kong is 31% and Thailand is 29%. A strong savings rate usually goes with a strong currency. In the last five years the Singapore dollar has doubled against the US dollar.

* *

About Clinton's "changes" and reforms. Basically what he's doing is taking money away from the efficient private market and putting it into the inefficient government workplace. If I were president, I would do only two things. First, I would back the dollar with gold -- make the dollar totally convertible into gold. Second, I would institute a national sales tax, while dumping every other federal tax (personal and corporate). The result would be a rock-hard dollar, the end of inflation, a booming economy and rising stock and bond markets. The problem -- those two actions would take a tremendous amount of power OUT of the hands of the politicians. So my two changes won't happen, short of an economic collapse.

* *

Jim Cook is president of *Investment Rarities* out of Minneapolis. Jim (like your editor) is a conservative, who doesn't believe that making life easy for individuals is the way to a nation's strength. In his latest report Jim writes: "Make no mistake about it, the US has embarked on two of the most incredible experiments in human history. America's combination of deficit spending, money creation, borrowing and debt dwarfs anything in history, and so there will be repercussions. The second great insanity lies with the behavioral consequences of giving people money they didn't earn. Nothing in history can compare with these two bizarre circumstances. Nothing even comes close. Quite possibly we are on the eve of the most astonishing period in history. For someone not to hedge against these two circumstances has to be the ultimate in a Pollyanna attitude."

Russell note: The ultimate hedge, of course is gold. In case you think the above is an extreme view, consider this: suppose there was no welfare in America? Suppose people actually had to take responsibility for their own actions. Would 1.1 million babies have been born out of wedlock in 1992 (as was the case)? Would young girls continue to think it was "in" or safe or fun to have illegitimate babies if the government wasn't there to pay the bills via welfare? And would people hit the unemployment office, pick up their pay, and then go home and watch TV? When I was unemployed as a young man I hit the streets, going door to door, asking for a job. Ah, that's another story from another era, but some day I'll write about it (Marty E., retired on Long Island, remember tramping the streets looking for work in '49? And hey, drop me a line, buddy).

The great Napoleon Hill wrote, *"When any individual reconciles himself to the state of mind wherein he is willing to accept largesse from the government instead of supplying his needs through personal initiative, that individual is on the road to decay and spiritual blindness."* President Clinton, meet Napoleon Hill.

* *

In an article entitled "Quantifying America's Decline" (*WSJ* op-ed page, Mar. 15), William Bennett writes, "Since 1960 the US population has increased by 41% . . . and total social spending by

all levels of government has risen from $143 billion to $787 billion, more than a five-fold increase . . . But during the same period there has been a 560% increase in violent crime; a 419% increase in illegitimate births; a quadrupling in divorce rates; a tripling in children living in single-parent homes; more than a 200% increase in the teen-age suicide rate; and a drop of almost 80 points in the SAT scores."

Russell comment: Let's face it, there's been a drastic decline in the quality of life in the US. Why? I've asked myself that question many times, and here's part of my conclusion. I firmly believe that the government has debased the American psyche via inflation, via a huge welfare program, via an expensive Social Security system that no one any longer trusts, by rising taxes that kill incentive, by a long list of institutions that relieves people of responsibility for their own actions. In the New America nobody has any responsibilities, everyone demands their rights, the courts are the pathway to riches, and morality falls apart.

* *

Baseball is still trying to figure out how to hire top-talent players, stay competitive and not go broke (baseball, stupidly, doesn't have a cap on team expenses). Basketball pays the monster salaries. Hakeem Olajuwon just got a contract which pays him $34 million over the next six seasons. David Robinson, the highest-paid basketball guy,will get $5.72 million this season. In football's new free agency race, the hottest guy around is defensive player Reggie White. White is now touring six clubs in order to find the deal he likes best. The Cleveland Browns provided visiting Reggie with a private jet, a luxury hotel suite and a limo. In Atlanta Reggie met the governor, got a standing ovation from the state legislators and was handed a free steak dinner. Ah, to be a star athlete with a contract coming up. Wait, you think these guys are overpaid? Listen, Arnold Schwarzenegger gets $15 to $20 million a picture. In our capitalistic system, the market tells you what you're worth. Now as for corporate CEOs . . .

* *

Many Federal Reserve governors (and Richard Russell) are still stewing about Fed Chairman Alan Greenspan's chumminess with the Clinton administration. Former Fed chief Paul Volcker has also been privately critical of Greenspan's coziness. Volcker tells friends that when Ronald Reagan wanted to visit the Fed marble headquarters, he issued a flat statement to the president -- "No."

* *

If you're over 65 and want a real US tax haven, it's got to be Juneau, Alaska. The elderly are exempt from Juneau's 4% sales tax. Alaska also offers a tax exemption on the first $150,000 of valuation on a house. And oh yes, Alaska has no state income or sales tax. But oh, those winters.

* *

Speaking of taxes, in the last Letter I advocated a national sales tax which would replace our current tax system and which would put the great American tax industry out of business. Friend Bert Dohmen of *Dohmen Capital Group* writes, "It's extremely important to point out that the national sales tax should replace the personal income tax. It should not be in addition to! As you know, politicians would love to give us an additional tax. In Canada, the sales tax imposed a few years ago has now brought in more tax revenues than they had ever expected, even in an economy with 11.5% unemployment. But as you know, that sales tax was on top of the income tax. While pols are happy with the huge tax revenues collected, they don't realize that they are bleeding the patient to death."

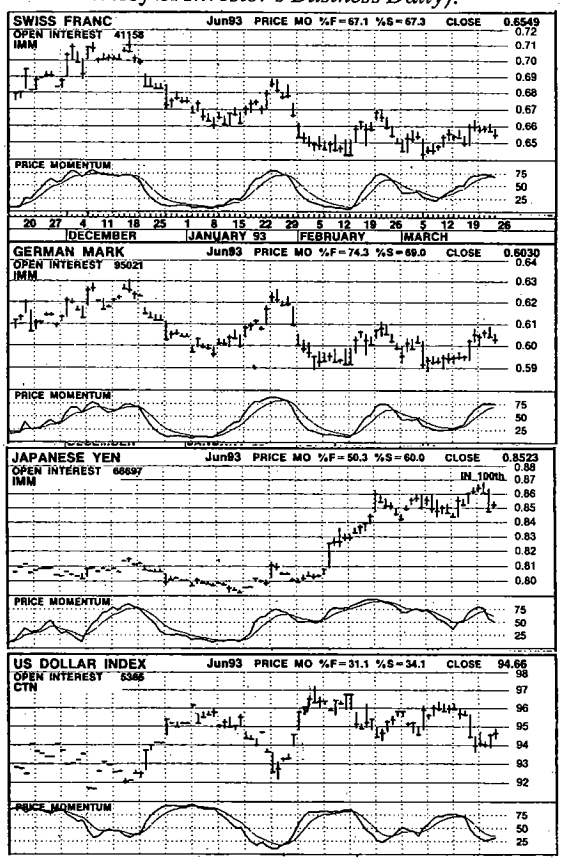
By the way, the Clinton administration has put out a feeler to the effect that they might ask for a national sales tax (on top of every other tax) to finance Hillary's top-secret national health plan. A national energy tax, higher personal taxes, a national sales tax, higher corporate taxes, I mean are things getting crazy or what?

* *

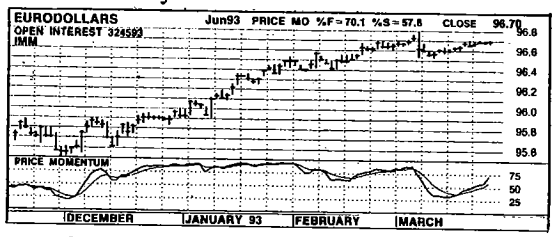
Over the last three years, one million Californians have moved out of the state, the majority (about 600,000) into the 11 other Western states. Last year government spending on MediCal jumped 36% in California. Total fed and state MediCal expenses in California last year reached $12.3 billion, up $3.3 billion for the year. MediCal expenses, among other things, are busting this state. Following the budget cuts of last year, California is still running a budget deficit of $8 billion. Governor Pete Wilson, who thought the governorship of the Golden State would be the path to the presidency, is finding out differently.

As for California's housing cave-in, last year alone the state chalked up a 30% collapse in housing starts, a 15% to 25% drop in housing prices, and a 40% jump in business failures. In the last two years, 21,550 real estate agents have simply vanished from the rolls of the California Association of Realtors.

ODDS 'n' ENDS: After seven months of the highest volatility in their history (to a large extent reflecting the collapse of the European Rate Mechanism), I now believe the currencies are going to simmer down and lapse into trading ranges. The stochastics ("price momentum" on the charts below) on the D-mark and the Swissie are indicating that these two are overbought, which lends substance to my trading range thesis. The yen, having surged in February, is also correcting, and I expect it to probe lower levels (all charts courtesy of *Investor's Business Daily*).

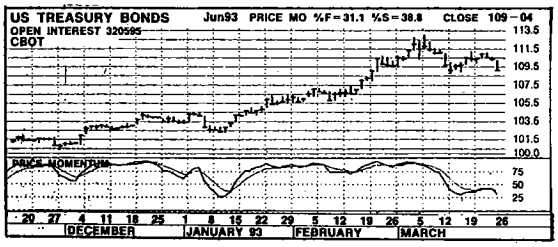


Meanwhile, the dollar has already corrected a bit, but here I expect a somewhat lower trend and then a trading range. If you're going to Britain, the buck will do more for you than it did for Faye and me when we visited London a few years ago. (The pound was then worth over $1.80. Since then it has come down to 1.40, then rallied to the 1.46-1.47 range.) I'm stubborn; personally, I think the pound is only worth a buck and a quarter if that. Why should I pay five dollars for a breakfast in Britain when I can get a better one here for three-fifty?



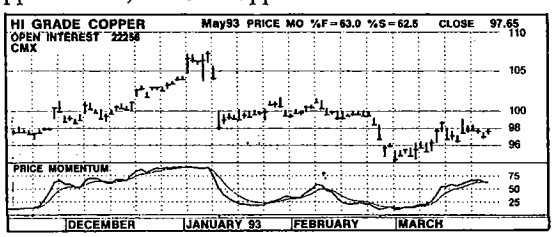
The key to short-term interest rates is the Eurodollar. Euro deposits are simply dollar deposits situated in overseas banks. But this is a totally free market and sophisticated investors watch it for the true trend of short rates in the dollar. As you can see, the Euros have enjoyed a huge rise from the December lows, meaning that short rates have been declining. The June contract is respecting the 96.5

level. If 96.5 is violated, however, it will signal short rates rising, an event that would be greeted with great distaste by the stock market and the economy .

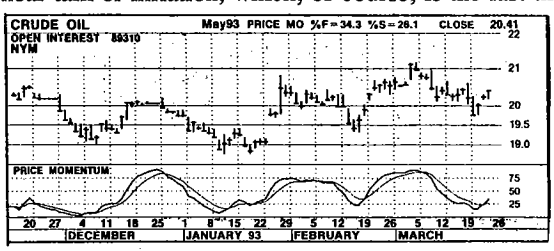


The long T-bond has also had a big advance, and here the critical level is 108.5 on the June contract. I'd be very surprised if the bonds made new highs, but they could be going into a trading range. If the market doesn't like what Clinton is doing, the bonds will break under 108.5. And if that happens, believe me, Clinton won't like what the bonds are doing. The bonds are really the key to the housing market, since mortgage rates trade off the bonds. As I said, **108.5** on the June contract is the level that must hold.

Industry uses lots of copper, and therefore the metal has barometric properties as far as the economy is concerned. Here's the chart of the May contract, and it's not particularly inspiring. Copper has been declining in steps ever since January. If there is a forthcoming building boom or car-selling explosion, it should show in the price of copper. So far, it hasn't happened.

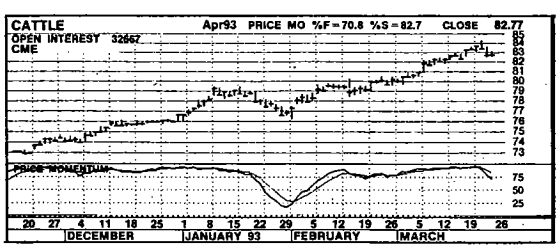


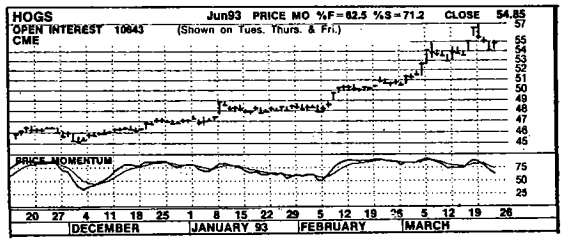
"Black gold," that's what they call oil. Since January we've had a rather subtle pattern of higher bottoms and higher tops. A new high would entail an advance well above $21 a barrel. If that happens, you'll hear talk of inflation, which, of course, is the last thing in



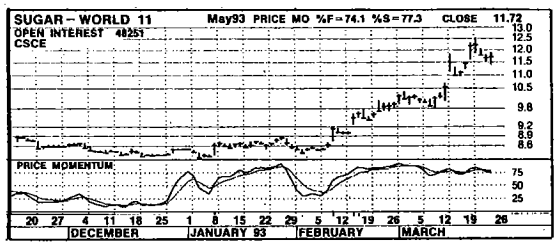
the world Alan Greenspan wants to hear. By the way, did you notice how Alan G. backtracked and reversed himself in his recent visit to Congress? Now he's saying that he never endorsed the Clinton program and that the Clinton crowd isn't coming up with enough budget cuts. Thanks Alan, that should help to cancel out your appearance next to Hillary at the State of the Union party.

Foodmaker may have served rancid hamburgers to the public, but those holding cattle contracts couldn't care less -- they've been making Watusi (that means BIG) bucks. Cattle contracts hit an all-time high in March. And the hogs did pretty well too. But more recently, it's been correction time. Nothing goes up forever (or down either) as every commodity trader knows only too well.



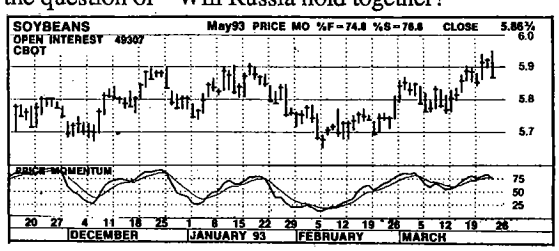


Sugar, it's been a sweet trade, actually (along with lumber) the best trade of the last few months. The price of sugar has been exploding since February, so it's been a dream trade for commodity traders (and a problem for bakers).

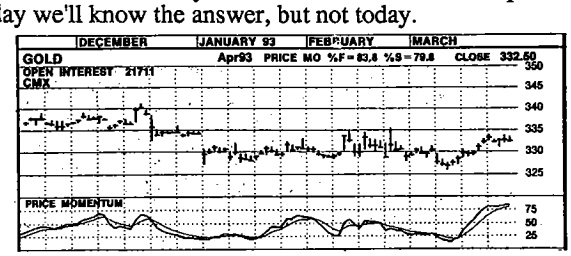


"Protein gold," that's what they call the grains. Two major crops are soybeans and corn. Both have been heading up with the beans looking like they want to go quite a bit higher. Commodity traders remember that old fantasy, "beans in the teens" (meaning beans at 13 cents or higher). Will that ever happen in our lifetime? I'll bet it will, but meanwhile bean bulls would settle on the May contract just rising to 6. Will that happen? I wouldn't bet against it. Those who follow the commodity cycles are saying that the commodities are at a five-year cyclical LOW. If they're right, look for a higher Consumer Price Index.

Inflation note: The Fed has purchased roughly $34 billion of bonds over the last 12 months. One report that I receive states that the Fed has been buying bonds at the rate of about $1 billion a week. So it isn't what Alan Greenspan is saying, it's what the Fed is DOING. I say they're monetizing the debt, trying to re-inflate, trying to offset the forces of deflation. Who'll win -- the downward forces of the Kondratieff Wave, or the re-inflation forces of the Fed? I can't tell yet, but here's a secret -- neither can anyone else. However, it's the number one question today, even bigger, I think, than the question of "Will Russia hold together?"



Last but not least, we have gold, which for the last three months has been in the tightest formation probably in history. Is it being manipulated? Or are buyers and sellers in absolute equilibrium? One day we'll know the answer, but not today.



LATE NOTES: The bull isn't through. The market wants to go higher, and this is confirmed by the pattern of the Averages, the continuing probe by the PTI into new high territory and certainly by the fact that the "Buying Stampede" is still in force. Since October 9, the A-D ratio has not registered a decline of as much as 1-point. The implication is clear -- there is an urgent desire by investors and the public to swap cash for stocks, regardless of low yields, higher taxes, the Russian siuation or anything else.

NEXT MAILING: April 14, 1993